Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 01-92
Developing a Unified Intercarrier	)	
Compensation Regime	)	

INITIAL COMMENTS OF MINNESOTA INDEPENDENT COALITION

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SUMMARY OF INITIAL COMMENTS OF MINNESOTA INDEPENDENT COALITION

The extraordinary scope and complexity of issues raised by the reform of intercarrier compensation will require the Commission to balance and prioritize critical policy objectives. In doing so, the Commission should take a pragmatic approach and focus on practical and timely steps that provide material progress toward the unification of intercarrier compensation rates, recognizing that different approaches and transitions are needed for Price Cap and Rate-of-Return ILECs. The key is for the Commission to prioritize. Preserving universal service and affordability of local rates should receive the highest priority from the Commission.

The Commission must also assume responsibility that corresponds to the scope of the changes that it initiates. More specifically, if the Commission requires reform of intrastate access rates and other intercarrier compensation (as it should), it is essential for the Commission to also provide mechanisms allowing replacement of the resulting reductions in revenue. The Commission cannot shift to the States the responsibility to provide necessary solutions to correspond to Commission required changes. Further, unless the Commission establishes the needed mechanisms, intercarrier compensation reform will be severely delayed, if not prevented. However difficult the implementation of Commission decisions affecting intrastate rates may be, the problems from delayed and inconsistent results that would result from state-by-state decisions would be worse.

In order to make timely progress, the Commission should accept the use of separate approaches and separate transitions for Price Cap ILECs and ROR ILECs because their financial characteristics, and the resulting financial impacts of reform, vary so widely. For example, available data indicates that intrastate access accounts for approximately 27% of the revenue of ROR ILECs in Minnesota and interstate access accounts for an additional 21%, both of which are far higher than for the Price Cap ILECs. If the Commission's decisions do not recognize and accommodate these differences, significant delays or harm to customers in rural areas will occur.

Given the potential for such significant financial impacts, and the fact that ROR ILEC intrastate access rates are typically substantially higher than their interstate access rates, the Commission's first priority for ROR ILECs should be to:

(1) reduce intrastate access rates to interstate access rates over a period of three or more years;

(2) prevent the gaps between access rates and reciprocal compensation from growing wider by implementing target reciprocal compensation rates;

(3) provide a mechanism for replacement of the resulting revenue reductions, which would include both: (i) reasonable and affordable Subscriber Line Charges increases ($1.50 per line per month in each year of the transition, up to individual Statewide Residential Rate Benchmarks that would be based on RBOC rates); and (ii) a new intercarrier compensation restructuring mechanism from which ROR ILECs could recover the balance of the intercarrier compensation reductions; and

(4) take steps to limit other arbitrage opportunities.

Further, ROR ILECs do not typically own the interexchange network facilities and are often far removed from tandems and other facilities of other indirectly interconnected carriers. The cost of providing transport beyond their local exchange networks would add substantially to their already much higher network costs. Accordingly, ROR ILECs should not be required to provide or pay for transport of traffic beyond their local exchange networks.

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The following Initial Comments are submitted to the Federal Communications Commission (the "Commission") by the Minnesota Independent Coalition ("MIC") in response to the Commission's FURTHER NOTICE OF PROPOSED RULEMAKING, CC Docket No. 01-92, released March 3, 2005 (the "*FNPRM*"). The MIC is an unincorporated association of over eighty small, Rate-of-Return Incumbent Local Exchange Carriers ("ROR ILECs") providing local exchange service to primarily rural areas in Minnesota. MIC members average approximately 4,800 access lines per company and range from less than 100 access lines to over 40,000 access lines. Fifty percent of the MIC members have fewer than 1,800 access lines. The average number of access lines per exchange for the MIC members is approximately 1,150, and 50% of the exchanges have less than 600 access lines.

These Initial Comments include a brief statement of principles that the MIC recommends for consideration by the Commission, along with specific recommendations and comments on some of the specific plans identified in the *FNPRM*. These Initial Comments will focus primarily on issues of concern to ROR ILECs in general and to MIC members in particular and are not intended to provide a complete alternative plan for intercarrier compensation reform. Rather, these Initial Comments are intended to identify factors that should be reflected in whatever plan the Commission adopts for ROR ILECs and to briefly compare some of the plans identified in the *FNPRM* to those factors.

I. PRINCIPLES

A. Reform of Intercarrier Compensation for ROR ILECs Will Require the Commission to Prioritize, Balance Policy Objectives, and Apply Pragmatic Approaches.

The policy goals for intercarrier compensation reform that have been identified by the Commission include: promotion of economic efficiency and facilities-based competition;[1] preservation of universal service, including particular emphasis on the needs of rural and high-cost areas;[2] promotion of regulatory certainty, minimization of regulatory intervention and minimization of arbitrage.[3] Given the sweep and inherent tension between some of these goals, particularly for ROR ILECs, the reform of intercarrier compensation will require the Commission to balance and prioritize important policy objectives. In doing so, the Commission should emphasize pragmatism and achievement of practical steps with measurable progress toward unification of intercarrier compensation rates. Finding the ultimate solution to *all*

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[1] *FNPRM* ¶ 31. "... Based on the record, we agree with commenters that any new approach should promote economic efficiency. ... Indeed, one of the Commission's most important policies is to promote facilities-based competition in the marketplace."

[2] *FNPRM* ¶ 32. "Preservation of universal service is another priority under the Act and we recognize that fulfillment of this mandate must be a consideration in the development of any intercarrier compensation regime. This Commission remains committed to universal service, and we are particularly sensitive to the interests of rural and high-cost communities." [Footnote omitted.]

[3] *FNPRM* ¶ 33. "... In addition, we favor an approach that provides regulatory certainty where possible and limits both the need for regulatory intervention and arbitrage concerns arising from regulatory distinctions unrelated to cost differences. Similar types of traffic should be subject to similar rules. Similar types of functions should be subject to similar cost recovery mechanisms."

intercarrier compensation issues for *all* carriers is likely an impossible challenge in the confines of this (or any other) single proceeding. However, that does not mean that achievement of complete, or nearly complete, solutions to some problems is not possible or that *substantial progress* cannot be achieved on many issues that may not be completely resolved. The key is for the Commission to prioritize.

The Commission should also recognize and accept that applying a uniform approach to all carriers is not feasible, because the situations and characteristics of carriers vary so widely. For example, the Commission has noted that ROR ILECs receive a far greater portion of their total revenue from access charges than do Price Cap ILECs.[4] In fact, access services provide an even greater portion of total revenues for many ROR ILECs.[5] The Commission has also noted that ROR ILECs have higher costs[6] and has recognized that it may be appropriate for ROR ILECs to maintain some level of compensation from IXCs.[7] Accordingly, it is clear that a solution that recognizes the unique circumstances of the ROR ILECs is needed. If the Commission's plan does not accommodate these differences, significant and unnecessary delays

[4] *FNPRM* ¶ 107. "As compared to price cap LECs, rate-of-return LECs derive a much greater share of their revenue from access charges."

[5] As discussed further in Section II.C.1.a., below, a sample of 40 Minnesota ROR ILECs obtained approximately 27% of total 2004 revenues from intrastate access services and 21% from interstate access services.

[6] *FNPRM* ¶ 32. "Because of the high costs associated with serving rural areas, we must be certain that any reform of compensation mechanisms does not jeopardize the ability of rural consumers to receive service at reasonable rates."

[7] *FNPRM* ¶ 112. "With respect to rate-of-return LECs in particular, we recognize that an approach that retains some intercarrier payments from IXCs for switched access services may be appropriate."

and harm to consumers, either in the form of high local rates or inadequate future services (e.g. broadband), will be likely.

Different solutions and different timetables have also been used in connection with prior Commission initiatives. The existence of Price Cap and ROR regimes and the *MAG Order*, *CALLS Order*, and *RTF Order* reflect such approaches,[8] as do the Commission's universal service rules.[9] The magnitudes and complexity of the issues facing the Commission in this proceeding similarly justify, if not compel, different approaches for Price Cap and ROR ILECs. In the area of intercarrier compensation, it is abundantly clear that "one size does not fit all."

As a result, there is both a need and a justification for a separate approach and separate transition for ROR ILECs.

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[8] SECOND REPORT AND ORDER AND FURTHER NOTICE OF PROPOSED RULEMAKING IN CC-DOCKET NO. 00-256, FIFTEENTH REPORT AND ORDER IN CC DOCKET NO. 96-45, AND REPORT AND ORDER IN CC DOCKET NOS. 98-77 AND 98-166, 16 FCC Rcd. 19613 (2001) ("*MAG Order*"); SIXTH REPORT AND ORDER IN CC-DOCKET NOS. 96-262 AND 94-1, REPORT AND ORDER IN CC DOCKET NO. 99-249, ELEVENTH REPORT AND ORDER IN CC DOCKET NO 96-45, 15 FCC Rcd. 12962 (2000) ("*CALLS Order*"); FOURTEENTH REPORT AND ORDER, TWENTY SECOND ORDER ON RECONSIDERATION, AND FURTHER NOTICE OF PROPOSED RULEMAKING IN CC-DOCKET NO. 96-45, AND REPORT AND ORDER IN CC DOCKET NO. 00-256, 16 FCC Rcd. 11244 (2001) ("*RTF Order*").

[9] 47 C.F.R. § 54.1 et seq.

B. Preventing Adverse Customer Impacts and Preserving the Comparability of Urban and Rural Rates Should Be Priorities.

The Commission recognizes that preventing adverse impacts on customers is a priority and that the combination of high costs of serving rural areas and the greater portion of revenues that ROR ILECs receive from access charges require particular attention from the Commission.[10] The Commission's concern is well founded. There are three potential sources for ILECs to recover network costs: (i) charges to local customers; (ii) charges to other carriers for use of those network facilities; and (iii) support mechanisms. ROR ILECs receive a far greater portion of total revenues from access services.[11] Without careful attention to impacts on rural customers, rate shock for rural customers or inadequate future service (e.g. the inability to deploy broadband) could easily occur as intercarrier compensation is reduced.[12]

The Act also expressly recognizes that urban and rural rates should remain comparable.[13] Maintaining comparability of urban and rural rates will require the Commission to establish

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[10] *FNPRM* ¶ 32. "Any proposal that would result in significant reductions in intercarrier payments should include a proposal to address the universal service implications, if any, of such reductions. In particular, many rural LECs collect a significant percentage of their revenue from interstate and intrastate access charges. Because of the high costs associated with serving rural areas, we must be certain that any reform of compensation mechanisms does not jeopardize the ability of rural consumers to receive service at reasonable rates."

[11] As discussed in Section II.C.1.a. below, a sample of Minnesota ROR ILECs received 48% of total 2004 revenues from access services (27% from intrastate and 21% from interstate).

[12] *FNPRM* ¶ *32* "[W]e seek comment in this item on universal service related issues raised by commenters, including the need to maintain reasonable and affordable end-user rates and the avoidance of rate shock."

[13] 47 U.S.C. § 254(b)(3) reads in part:

> Consumers … in rural, insular, and high cost areas, should have access to telecommunications and information services, … at rates that are reasonably comparable to rates charged for similar services in urban areas.

appropriate mechanisms to address the impacts of changes in both interstate and intrastate intercarrier compensation. For reasons discussed below, such comparability should be determined on a statewide basis and implemented in the form of Statewide Residential Benchmark rates.

C. <u>The Scope of the Commission's Responsibilities Corresponds to Changes Initiated by the Commission, Including Both Interstate and Intrastate Compensation and Compensation Restructuring Mechanisms.</u>

The scope of the Commission's responsibility must correspond to the scope of its decisions. If the Commission ventures into the area of intrastate access rates (as it should), the Commission must also assure that the other changes that are necessitated by its decision actually occur. The State Commissions can and should play a key role in assuring comparability of urban and rural rates. However, if the Commission chooses to establish requirements that apply to intrastate rates, including intrastate access rates, the Commission has the corresponding responsibility to establish criteria and take the steps needed to assure that comparability of rural and urban rates is maintained when those requirements are implemented in the 50 states.

The States have historically been responsible for intrastate access and intrastate local rates and revenues, and the Commission has historically refrained from exerting authority over intrastate access rates. The U.S. Supreme Court in *AT&T v. Iowa Utils. Bd.* determined that the Commission's rulemaking authority, provided by 47 U.S.C. § 201(b), extends to all provisions of the Act, including intrastate service to the extent it is covered by the Act, and that the 1996 Act removed significant areas from the States' exclusive control.[14]

[14] *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 377-86; 119 S. Ct. 721, 728-733 (1999) ("*AT&T v. IUB*").

The Commission has recognized the relationship between reductions in access revenues and replacement of those revenues with other sources and the particular significance of this issue for ROR ILECs.[15] Consequently, to the extent that the Commission exercises its authority over intrastate rates (which it should), the Commission must also assume corresponding responsibility for implementation of a complete solution to intercarrier access reform. That solution necessarily includes establishing replacement sources for reductions in intercarrier compensation in order to maintain comparable and affordable rates for rural consumers.

The *FNPRM* seems to suggest that if the States act to reduce intrastate access rates in response to a Commission directive, the Commission may be relieved of responsibility, even if the States are acting as directed by the Commission.[16] To the contrary, the issue is not which entity takes the final change, but *which entity initiates* the change. To the same extent the Commission initiates reductions of intrastate access rates and other intercarrier compensation, the Commission is responsible for implementation of a corresponding mechanism to replace the reductions in intrastate intercarrier compensation.

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[15] *FNPRM* ¶ 108. "Because many rate-of-return LECs depend so heavily on access charge revenue, some of the proposals submitted in this proceeding include special provisions for these carriers. ... We seek comment on the extent to which the Commission should give rate-of-return LECs the opportunity to offset lost access charge revenues with additional universal service funding, additional subscriber charges, or some combination of the two."

[16] *FNPRM* ¶ 115. "If the states reduce access charges as part of a comprehensive reform effort adopted by the Commission, issues may arise as to whether the Commission or the state is responsible for establishing an alternative revenue source. ... We seek comment on whether the Commission should create a federal mechanism to offset any lost intrastate revenues, or whether the states should be responsible for establishing alternative cost recovery mechanisms for LECs within the intrastate jurisdiction."

The inherent problems of delegation to State Commissions were recently articulated in *USTA v. FCC*[17]:

> When an agency delegates authority to its subordinate, responsibility—and thus accountability—clearly remain with the federal agency. But when an agency delegates power to outside parties, lines of accountability may blur, undermining an important democratic check on government decision-making. ... Also, delegation to outside entities increases the risk that these parties will not share the agency's "national vision and perspective," ... and thus may pursue goals inconsistent with those of the agency and the underlying statutory scheme. In short, subdelegation to outside entities aggravates the risk of policy drift inherent in any principal-agent relationship

The same is true in the present case.

Practical considerations also require that the Commission establish a nation-wide plan, including the development and implementation of replacement mechanisms, so that Commission mandated reductions to both interstate and intrastate access rates and other net intercarrier compensation reductions are replaced by alternative recovery sources. Several obstacles prevent reliance on individual States to both develop and implement replacement mechanisms. Some State Commissions lack the legislative authority needed to develop a mechanism to replace required reductions in intercarrier compensation. Other State Commissions lack the authority to require certain categories of carriers to participate and fund such a mechanism. Other State Commissions may disagree with the policy decisions made by the Commission and may, accordingly, not be inclined to cooperatively implement a Commission-developed policy aimed at intrastate rates. All of these possibilities raise the risk of contentious political, regulatory and legal contests in multiple States, with virtually no prospects for consistent, much less timely, outcomes to resolve the current intercarrier compensation problems. However difficult the legal

[17] *USTA v. FCC*, 359 F.3d 554, 565-66 (D.C. Cir. 2004).

and public policy issues and complexities resulting from Commission action may be, the legal and public policy problems and complexities posed by delayed and inconsistent results in 50 States are worse. If the Commission wants timely and consistent progress on intrastate access and other intercarrier compensation reforms, it must, as a practical matter, assume responsibility for assuring consistent solutions.

A nationwide plan is also needed for *predictability*, both for carriers doing business in multiple States and for carriers doing business in only one State. For carriers doing business in multiple States, the risk of inconsistent decisions will be applied to very substantial revenue sources (intrastate access rates and other intercarrier compensation). That risk would severely curtail investments during the years of uncertainty that would result from multiple legislative, regulatory, and legal contests in multiple States. Carriers doing business in only one State will experience the same type of uncertainty, even if they do not risk inconsistency. Predictability and reasonable certainty are essential to promote long-run investing in the rural, high cost areas served by ROR ILECs. The required level of predictability and certainty can result only from a nationwide plan.

Finally, arbitrage can be addressed effectively only through a nationwide plan. Arbitrage is largely the result of regulatory lag and inconsistency. To the extent that there are multiple State plans, the occasions for inconsistency (and hence, arbitrage) are similarly multiplied. Such a result would defeat the policies that the Commission seeks to establish.

D. <u>A Different Approach and Different Transition Are Needed for ROR ILECs.</u>

A different approach to intercarrier compensation reform is needed for ROR ILECs because of the substantial differences between ROR ILECs and Price Cap ILECs. There are three potential sources for ILECs to recover network costs: (i) charges to local customers; (ii) charges to other carriers for use of those network facilities; and (iii) support mechanisms. ROR ILECs need a different balance between these three potential sources of network cost recovery than the Price-cap ILECs do in order to maintain affordable rates and to continue to invest in critical network facilities.

The Commission has recognized that ROR ILECs have significantly higher network costs than Price Cap ILECs.[18] These higher network costs of ROR ILECs, combined with the legal and policy objectives to keep local charges affordable and preserve comparable statewide urban and rural rates, require ROR ILECs to rely more on intercarrier compensation[19] and support mechanisms.[20] Some portion of these higher rural network costs must be recovered by intercarrier compensation for the foreseeable future in order to prevent unsustainable local rate increases and to limit demands on support mechanisms.[21]

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[18] *FNPRM* ¶ 32. "Because of the high costs associated with serving rural areas, we must be certain that any reform of compensation mechanisms does not jeopardize the ability of rural consumers to receive service at reasonable rates."

[19] *FNPRM* ¶ 112. "With respect to rate-of-return LECs in particular, we recognize that an approach that retains some intercarrier payments from IXCs for switched access services may be appropriate."

[20] *FNPRM* ¶ 108. "Because many rate-of-return LECs depend so heavily on access charge revenue, some of the proposals submitted in this proceeding include special provisions for these carriers. ... We seek comment on the extent to which the Commission should give rate-of-return LECs the opportunity to offset lost access charge revenues with additional universal service funding, additional subscriber charges, or some combination of the two."

[21] As a result, the ICF bill and keep proposal should not be adopted for ROR ILECs.

Unless these higher network costs are recoverable, ROR ILECs will be unable to maintain existing investments and make further investments needed to maintain service quality and to insure availability of broad-band networks and the services that require a broad-band network. For example, broadband deployment cannot be achieved by 2007[22] unless ROR ILECs have a reasonable opportunity to recover their network costs. Continued investment in rural infrastructure and the state-of-the-art services that result are more essential than ever to the economic vitality of rural areas.

The Commission has recognized the need for transition, and that the need for transition increases as the scope of change increases.[23] The Commission has also recognized that different transition periods may be needed for Price Cap and ROR ILECs.[24] Given the substantially larger portion of total revenues that ROR ILECs receive from access charges, the need for a separate transition period is needed to preserve the affordability and comparability of local services and rates in rural areas as compared to urban areas.

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[22] CNET Newscom, April 26, 2004.

[23] *FNPRM* ¶ 36. "[T]here will be numerous implementation issues associated with any significant reform of intercarrier compensation mechanisms. ... [T]o the extent a proposal includes significant changes in the level of compensation carriers might receive, we would expect to see a detailed transition plan that will give carriers time to adjust their business plans."

FNPRM ¶ 117. "Many of the proposals submitted in this record include some sort of transition period to give carriers sufficient time to make necessary changes in their business operations. Given the substantial changes that are possible in this rulemaking, we seek comment on what type of transition would be needed for a new regime. ... Parties should be specific in proposing time frames and milestones that would be part of any transition to a new access charge regime."

[24] *FNPRM* ¶ 118. "Parties also should address whether there are any adverse consequences associated with transitioning rate-of-return LECs toward a new unified regime at a slower pace than price cap LECs."

An appropriate transition for ROR ILECs would first address the highest priority issues for ROR ILECs and prevent worsening of other issues, and subsequently resolve other issues. Significant progress can be promptly achieved, even if subsequent steps are needed. Further, the compounded complexity of attempting to simultaneously address *all* issues will impede, if not prevent, timely progress on *any* issues. As further discussed below, the very significant and difficult issue of intrastate access reform for ROR ILECs should be addressed in the initial phase of this process. While intrastate access reform is occurring, the Commission should implement rules that prevent the current problems the Commission has recognized (gaps between reciprocal compensation and access rates and arbitrage) from becoming worse.

II. SPECIFIC RECOMMENDATIONS

A. <u>The FCC Should Establish a Consistent, Nationwide Plan That Includes Intrastate Access Rates and Reciprocal Compensation Rates and a New Intercarrier Compensation Restructuring Mechanism.</u>

The Commission has the authority to establish a consistent nationwide plan addressing both interstate and intrastate intercarrier compensation issues. The Commission should also establish and implement a corresponding intercarrier compensation restructuring mechanism that includes both interstate and intrastate compensation. State execution of a Commission plan of intercarrier compensation restructuring would not lessen the Commission's responsibility to establish a mechanism that addressed intrastate compensation.

1. The Commission has authority to address intrastate access and reciprocal compensation and to adopt a corresponding intercarrier compensation restructuring mechanism to replace affected revenue sources.

The FCC has legal authority over intrastate matters, including intrastate access charges. In *AT&T v. Iowa Utilities Board*[25], the United States Supreme Court held that the Commission's rulemaking authority is not limited to interstate matters, but extends to all matters under the Act, including matters that were within the exclusive jurisdiction of the States prior to 1996, and is not limited to interstate matters. The Act was clearly intended to facilitate competition, including competition for local and interstate and intrastate interexchange services. Further, Section 254(g) requires the Commission to adopt rules assuring that both interstate and intrastate toll rates remain geographically averaged.[26] The Act's promotion of both interstate and intrastate competition and preservation of geographically averaged intrastate toll rates support the Commission's authority in regards to intrastate access rates. The significant discrepancies between interstate and intrastate access rates are becoming an obstacle to competition and to the preservation of geographically averaged toll rates. The Commission's authority to adopt rules to carry out the purposes of the Act includes rules that address intrastate access rates.

Further, the effect of intrastate access rates on arbitrage and, as a result, on interstate traffic also provides a basis for Commission authority. In *Louisiana Pub. Serv. Comm'n v. FCC*[27] the United States Supreme Court recognized that the FCC has authority if contrary State

[25] *AT&T v. IUB,* 525 U.S. at 377-86; 119 S. Ct. at 728-733.

[26] The Commission adopted 47 C.F.R. § 64.1801 in fulfillment of that obligation which requires geographic rate averaging of both intrastate and interstate interexchange telecommunications services.

[27] Louisiana Pub. Serv. Comm'n v. FCC, 476 U.S. 355 (1986).

regulations would "negate" legitimate federal regulation. Given the increasing difficulty of determining the jurisdiction of traffic, the effect on arbitrage, and the adverse effects of arbitrage on federal policy, the Commission is fully justified in including intrastate access rates within its plan to reform intercarrier compensation.

2. A new intercarrier compensation restructuring mechanism should correspond to all intercarrier compensation reductions that the Commission requires.

If the Commission mandates interstate and intrastate intercarrier compensation reductions, the Commission has an obligation to establish a corresponding intercarrier compensation restructuring mechanism that will provide an opportunity to replace the portion of revenues: (i) that are lost by carriers as a direct result of decisions made by the Commission; and (ii) that cannot be recovered from local customers without causing unreasonable rate increases. The new mechanism needs to cover both interstate and intrastate intercarrier compensation to the same extent that the Commission's decision requires reductions to interstate and intrastate intercarrier compensation, including any Commission mandated reductions of interstate access and other revenues below a ROR ILEC's interstate revenue requirement. The absence of such a mechanism would impose a mandate on the States without the funding needed to accomplish the mandate. The absence of such a mechanism would also lead to either (or both) of: (i) the loss of comparable urban and rural rates; and (ii) the failure of the effort to reform intercarrier compensation. The mechanism would be directed solely to revenue reductions resulting from the Commission's decision in this proceeding and would not replace the current federal USF or any existing State universal service support mechanisms.

3. State implementation of Commission established requirements would not diminish the Commission's responsibilities.

As previously noted, the *FNPRM* suggests that the Commission may not be responsible to establish a mechanism that would include intrastate access revenue reductions if the States implement the specific reductions as part of an overall plan established by the Commission.[28] To the contrary, the Commission's responsibility corresponds to the scope of its decision irrespective of whether the States perform an intermediate step of executing that decision. Several practical considerations also require the Commission to implement a new intercarrier compensation restructuring mechanism. State Commissions may lack the statutory authority to establish mechanisms to address access and/or reciprocal compensation rate reductions, or to assess some (or all) categories of carriers to fund such mechanisms. In particular, many State Commissions lack any authority over CMRS providers, including authority to require provision of funding. Other State Commissions may have varying levels of authority and multiple regulatory patterns applicable to the ILECs and CLECs doing business in their States, which may also impede State Commission implementation of a Commission policy.[29] Some ILECs are also subject to State obligations, often in connection with alternative forms of state regulation, that

[28] *FNPRM* ¶ 115. "If the states reduce access charges as part of a comprehensive reform effort adopted by the Commission, issues may arise as to whether the Commission or the state is responsible for establishing an alternative revenue source. ... We seek comment on whether the Commission should create a federal mechanism to offset any lost intrastate revenues, or whether the states should be responsible for establishing alternative cost recovery mechanisms for LECs within the intrastate jurisdiction."

[29] In Minnesota, there are distinctions between the Minnesota Public Utilities Commission authority over "independent telephone companies" (i.e., ROR ILECs) and larger ILECs and between member of those categories (based on whether the ILECs are subject to "alternative forms of regulation" [i.e., price-cap]) and Competitive Local Exchange Carriers.

preclude the ILECs from initiating increases in local charges for varying periods of time.[30] Implementation of intercarrier compensation reductions and authorization of increases in end user rates to recover even a portion of the reduction in intercarrier compensation would be a highly sensitive public policy issue. This is likely to make consistency between States virtually impossible to achieve and is almost certain to create substantial delays. Multiple legislative, regulatory, and legal contests would undoubtedly result, leading to fragmentation and/or grid-lock of the intrastate side of the reform effort. While some may argue that such results would be the sole responsibility of the States and should not be a source of concern to the Commission, the chaotic results that follow would impede implementation of the Commission's decision, prevent needed investment, and be ultimately self defeating.

Further, the only way to defer the responsibility for establishing necessary mechanisms to the States is to also defer the basic decision of whether to adjust intrastate rates and compensation levels to the States. That approach is inappropriate because the same fragmentation and grid-lock would result.

B. Intrastate and Interstate Access Rates and Reciprocal Compensation for ROR ILECs Should Be Reformed, But Not Replaced With Bill and Keep.

The Commission has recognized that the characteristics of the ROR ILECs may require retention of intercarrier compensation for the ROR ILECs.[31] The Commission is correct in this conclusion. Instead of imposing bill and keep regime for ROR ILECs, the Commission should

[30] E.g., Minn. Stat. §§ 237.76-769 and 237.774.

[31] *FNPRM* ¶ 112. "With respect to rate-of-return LECs in particular, we recognize that an approach that retains some intercarrier payments from IXCs for switched access services may be appropriate."

establish target rates for ROR ILECs' interstate and intrastate access charges (based on the embedded costs used to establish interstate access rates) and for reciprocal compensation.[32]

1. Replacing access charges and reciprocal compensation with bill and keep would prevent ROR ILECs from maintaining their high cost networks at affordable local rates.

Replacing access charges and reciprocal compensation with bill and keep would be generally inappropriate for ROR ILECs because it would not provide sufficient revenues to maintain robust networks and affordable local rates in rural and high cost areas, much less rates that are comparable to urban rates, or to provide quality service or network enhancements.[33] The Commission has recognized that ROR ILECs have significantly higher network costs than Price Cap ILECs, and receive substantially more of their revenue from access charges.[34] In contrast, the combination of: (i) appropriate target rates for interstate and intrastate access and reciprocal compensation; (ii) reasonable increases in local charges; and (iii) support from a new mechanism would meet these objectives.

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[32] The EPG and ARIC plans recognize that access rates for ROR ILECs should continue to be based on embedded costs.

[33] The ICF plan contains a number of proposals worthy of consideration, but its abandonment of much of the current intercarrier compensation mechanisms (e.g., originating access and terminating switching) for ROR ILECs and over reliance on replacement funding mechanisms should not be adopted. Nor should reciprocal compensation replace other established facility funding arrangements for extended area service.

[34] *FNPRM* ¶ 32. "Because of the high costs associated with serving rural areas, we must be certain that any reform of compensation mechanisms does not jeopardize the ability of rural consumers to receive service at reasonable rates."

FNPRM ¶108. "Because many rate-of-return LECs depend so heavily on access charge revenue, some of the proposals submitted in this proceeding include special provisions for these carriers. ... We seek comment on the extent to which the Commission should give rate-of-return LECs the opportunity to offset lost access charge revenues with additional universal service funding, additional subscriber charges, or some combination of the two."

The Act and past Commission decisions have strongly encouraged new investment in rural service areas, which has supported the goal of universal service.[35] In 2004, 97.8% of Minnesota households had telephone service.[36] In order to continue the investments needed to support universal service, ROR ILECs need to have a predictable and sufficient source of revenue. Bill and keep would not provide a sufficient source of revenue to enable affordable and comparable rural rates or network maintenance, much less network enhancement. Use of TELRIC or another forward looking or incremental cost methodology to determine access and reciprocal compensation rates for ROR ILECs would prevent predictability. Carriers cannot be expected to invest in the future when they cannot reasonably determine the sources and amounts of revenues. To establish a reasonable level of predictability and insure continued investment in rural infrastructure, the Commission should establish the rates for both interstate and intrastate access and reciprocal compensation for ROR ILECs.

2. TELRIC does not provide an appropriate basis for ROR ILEC access rates.

The Commission has asked whether TELRIC or other forward looking costs should be used to develop rates for ROR ILECs.[37] Using TELRIC or other forward looking cost to develop a uniform access rate for ROR ILECs would be inappropriate because, as the Commission has concluded, there is no forward-looking cost model that has been proven to be accurate for ROR

[35] The Commission has noted the importance of promoting infrastructure investment and broadband deployment in the *Report and Order and Order on Remand and Further Notice of Proposed Rulemaking*, CC Docket No. 01-338, Released August 21, 2003 and *Memorandum and Order*, Docket No. 01-338, Released October 27, 2004.

[36] *Telephone Penetration By Income By State*, Industry Analysis and Technology Division, Wireless Competition Bureau, (Released: March 2005).

[37] *FNPRM* ¶¶ 71-73.

ILECs.[38] Instead, the Commission concluded that an embedded cost basis remained appropriate basis for determining the level of USF revenues needed to support universal service goals because a greater portion of their total revenues was received from universal support mechanism.[39] The same conclusion applies here with respect to access charges.

Developing an appropriate forward-looking cost model, selecting appropriate inputs in the context of rapidly changing technology, and running and maintaining the cost model would be prohibitively expensive and lead to significant delays. Further, application of such a model would present a significant risk that the revenues needed to foster investment in rural telecommunications would not be provided. In addition, implementation of a TELRIC cost study for all ROR ILECs would very likely lead to ongoing regulatory and legal disputes regarding appropriate inputs and the traffic sensitivity of various costs. The resulting delay makes the development of separate TELRIC rates for the over 1,000 ROR ILECs totally impractical.

3. Reciprocal compensation should not be required for ROR ILECs in connection with expanded local calling areas or in connection with dial-up ISP traffic.

Many existing local calling arrangements that involve more than one ILEC's service area were based on bill and keep arrangements, and existing local rate structures were developed based on those arrangements. In Minnesota, (and many other states) such calling arrangements

[38] *RTF Order* ¶ 25. "The present record fails to provide the analysis necessary to permit a transition of rural carriers to a forward-looking high-cost support mechanism. Before we could transition to such a mechanism, it would need to be fully analyzed and considered. Even commenters who urge the commission to move toward a forward-looking support methodology for rural carriers as soon as possible recognize the need for additional time to develop an appropriate mechanism."

[39] *Id.* "In the meantime, providing support based on embedded costs will provide important certainty to rural carriers, which generally receive a greater portion of their revenues from universal support mechanisms than non-rural carriers."

are referred to as "Extended Area Service" ("EAS") and are very common, have been in existence for substantial periods of time, and involve substantial areas. The Minneapolis/St. Paul EAS area has been in existence since the 1950's, has been expanded many times since then, and provides local calling to over 2,000,000 access lines. Over 95% of access lines in Minnesota have some EAS. Most EAS service has an additional and separately identified charge and is provided on a non-optional basis as the result of customer votes and/or Minnesota Commission orders. Rates for EAS have been established to include access revenues that were eliminated as a result of expanding the local calling areas. Implementing reciprocal compensation for existing EAS traffic[40] would cause a significant and unreasonable change in those financial arrangements and effectively require repricing of EAS, disrupting service to the vast majority of customers in Minnesota.

Applying reciprocal compensation to traffic from ROR ILECs to ISP providers that are served by CLECs or other ILECs and located outside of the ROR ILECs' local exchange areas would have the same potential. ISPs are able to serve the entire Minneapolis/St. Paul EAS area by establishing their businesses locations within a single exchange. Virtually all of these ISPs have, not surprisingly, established their business locations in the central exchange areas of Minneapolis and St. Paul. The result has been a growing, very substantial imbalance of traffic flowing from the ROR ILECs to the central exchange areas of Minneapolis and St. Paul. If the Commission were to require reciprocal compensation for this traffic, it would have a huge, adverse financial impact on the outlying ROR ILECs, virtually requiring re-pricing of service to their customers. Further, such an arrangement for ISP traffic would also encourage arbitrage.

[40] The ICF Plan appears to require transiting charges for at least a portion of the traffic within expanded local calling areas, including EAS areas.

Accordingly, it is imperative that the Commission reinstate its prior policy of handling ISP traffic on a bill and keep basis, at least with respect to ROR ILECs.

C. A Separate Transition Process and Period Are Needed For ROR ILECS.

The financial consequences on ROR ILEC end-use customers of unifying interstate and intrastate access charges for ROR ILECs would be significantly greater than on Price Cap ILECs. In recognition of that impact, a phase in period of at least three years should be used to both: (i) reduce intrastate access rates for ROR ILECs to interstate levels and to interstate rates for ROR ILECs; and (ii) implement the increase of end user customer charges that would result. The Commission has previously applied separate timetables for ROR ILECs.[41] These transitions would not only lessen rate shock, but also limit the level of support needed during the transition. The Commission has also recognized the need for transition[42] and that a separate transition would likely be needed for the ROR ILECs.[43]

The transition plan for ROR ILECs should: (i) substantially reduce discrepancies in intercarrier compensation by implementing uniform intrastate and interstate access rates and setting a reasonable interim default rate for reciprocal compensation; (ii) take reasonable steps to

[41] See. *MAG Order* and *CALLS Order*.

[42] *FNPRM* ¶ 36. "[T]o the extent a proposal includes significant changes in the level of compensation carriers might receive, we would expect to see a detailed transition plan that will give carriers time to adjust their business plans."

[43] *FNPRM* ¶ 118. "Parties also should address whether there are any adverse consequences associated with transitioning rate-of-return LECs toward a new unified regime at a slower pace than price cap LECs."

limit other arbitrage opportunities and discrepancies; and (iii) remove obstacles to negotiating reciprocal compensation agreements by establishing reasonable reciprocal compensation rates.

1. Intrastate access rates should be reduced to interstate levels and reciprocal compensation defaults and benchmarks should be established and applied.

The MIC recommends a phase-in of at least three years during which: (i) ROR ILECs interstate and intrastate access rates would be unified at interstate levels; and (ii) the Commission would establish default benchmark reciprocal compensation rates. Specifically, during the transition period:

- *Intrastate Access Rates:* ROR ILEC intrastate access rates would be phased down to their interstate access rate levels in equal annual steps;
- *Interstate Access Rates:* ROR ILEC interstate access rates would continue to be based on embedded costs and ROR ILECs would continue existing pooling arrangements for interstate access revenues and costs;
- *Reciprocal Compensation*: A uniform reciprocal compensation rate would be established for ROR ILECs at the lower of: (i) the target level (e.g. $ .015 to $.02 cents per minute) plus an additional amount for lengthy transport routes; or (ii) any rate mutually agreed to in interconnect negotiations. ISP traffic would not be subject to reciprocal compensation;
- *Statewide Residential Benchmark:* Each State Commission would determine its Statewide Residential Benchmark pursuant to Section IV. D. below;
- *Additional SLCs*: ROR ILECs would implement additional SLCs, subject to appropriate annual and cumulative caps to prevent excessive charges and rate shock to end users, and

receive support from a new intercarrier compensation restructuring mechanism, as discussed in Section IV.A.4 below; and

- *Further Steps:* The Commission would further consider the feasibility of unifying reciprocal compensation and access rates following the transition period.

A transition of at least three years is appropriate for ROR ILECs because the consequences of attempting a unification at a faster pace would lead to one (or a combination) of three consequences: (i) unsustainable local rate shock would be imposed on ROR ILEC customers[44]; (ii) ROR ILECs would be deprived of essential financial resources needed to maintain and enhance network facilities;[45] or (iii) immediate and very substantial increased demands would occur on the new intercarrier compensation restructuring mechanism.

a. Reducing ROR ILECs' intrastate access rates to interstate levels would remove a significant disparity, reduce arbitrage, and involve very substantial revenues.

Currently, most ROR ILECs' intrastate access rates are significantly higher than their interstate access rates. Because of the significant financial consequences of reducing intrastate access for most ROR ILECs, a transition to a uniform interstate and intrastate access rate should occur over a period of at least three years.

The use of interstate rates as a target for intrastate rates would be practical, efficient to administer, and substantially reduce the costs of providing interexchange service while still

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[44] *FNPRM* ¶ 32. "[W]e seek comment in this item on universal service related issues raised by commenters, including the need to maintain reasonable and affordable end-user rates and the avoidance of rate shock."

[45] *Id.* ¶ 107. "As compared to price cap LECs, rate-of-return LECs derive a much greater share of their revenue from access charges."

providing a reasonable level of compensation from IXCs. A transition would allow the maintenance of affordable local rates while limiting the cost of the new mechanism.

Using interstate access rates for all ROR ILECs' access rates would eliminate the most significant disparity in intercarrier compensation levels, reduce arbitrage, and substantially reduce the costs of providing interexchange services. Such a step would facilitate subsequent efforts to unify access rates and reciprocal compensation rates.[46] Phasing intrastate access rates to interstate levels would minimize delay, and maximize administrative efficiency because there would be no need to develop additional cost studies or conduct additional proceedings.

The transition is needed because of the very substantial portions of total revenue that are received from access charges by many ROR ILECs.[47] For example, a review of 2004 revenues for 40 ROR ILECs in Minnesota (for which data was available) showed that:

- intrastate access accounted for an average of 27% of total revenue; and
- interstate access accounted for an average of 21% of total revenue.
- that total access accounted from 48% of total revenues.

Eliminating 48% of revenues (by imposing bill and keep in place of access charges) would have a devastating effect on the ROR ILECs in Minnesota. Phasing out more than the difference

[46] The EPG and ARIC plans are consistent with the MIC recommendation of supporting the eventual unification of intrastate and interstate access rates and reciprocal compensation rates. However, the ICF plan, which appears to achieve unification at the unacceptable price of a bill and keep arrangement, is fundamentally inconsistent with the MIC recommendation.

[47] *FNPRM* ¶ 107 "According to NTCA, rural LECs receive on average, 10 percent of their revenue from interstate access charges and 16 percent from intrastate access charges. In comparison, it asserts that the BOCs receive only four percent of their revenue from interstate access charges and six percent from intrastate access charges."

between the interstate and intrastate access rates in the initial three years would pose substantial challenges.

Unifying intrastate and interstate access rates would eliminate substantial arbitrage opportunities and disputes. Because intrastate rates are generally higher than interstate rates, IXCs would experience significant reductions in the costs of providing interexchange services in rural areas.

b. A reasonable default reciprocal compensation rate is needed to prevent the gap between access rates and reciprocal compensation rates from widening.

The Commission has asked what obstacles impede the use of contracts as the mechanism for establishing intercarrier compensation arrangements for ROR ILECs.[48] The Commission also asked what the default compensation rule would apply in the absence of an agreement.[49] If the Commission wishes to facilitate negotiations, and the payment of reciprocal compensation by CMRS carriers,[50] it needs to resolve the dilemma posed by TELRIC-based rates to the negotiation process. The establishment of a reasonable default reciprocal compensation rate would accomplish both of these objectives.

The MIC's experience in negotiations with CMRS carriers demonstrates the need for a Commission established reasonable default rate and the inherent problems of attempting to use

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[48] *FNPRM* ¶ 116. "We ask parties to identify any unique obstacles that may arise for rate-of-return LECs in connection with a regime based solely on agreements and to propose solutions to overcome those obstacles."

[49] *Id.* "What would be the default compensation rule if parties exchanged traffic in the absence of some type of interconnection agreement?"

[50] *T-Mobile et al. Petition for Declaratory Ruling Regarding Incumbent LEC Wireless Termination Tariffs,* DECLARATORY RULING AND REPORT AND ORDER, 2005 WL 433200, FCC 05-42, CC Docket No. 01-92, February 24, 2005.

TELRIC-based reciprocal compensation rates for ROR ILECs, particularly for the relatively small quantities of traffic handled by ROR ILECs. The unavailability of a generally accepted TELRIC model for ROR ILECs and the cost of completing TELRIC studies have largely prevented ROR ILECs from using arbitration as a means to resolve negotiation deadlocks and has given CMRS carriers significant and unreasonable negotiating power. Unlike most ROR ILECs, most CMRS providers are large regional or national carriers with the financial ability to support permanent cost-study, negotiation teams, who are able, under present circumstances, to dictate unreasonably low rates for small ROR ILECs. Further, the CMRS providers' advantage is enhanced because CMRS providers are not required to provide cost studies in support of the rates that they demand.

To overcome this substantial obstacle to the use of negotiated agreements, the Commission should establish reasonable default reciprocal compensation rates for ROR ILECs. During the transition period (during which intrastate access rates are transitioned to interstate rate levels) reciprocal compensation rates for an ROR ILEC should be established at the lower of: (i) a Commission established default target (e.g., \$ .015 to \$.02 cents per minute), plus an additional amount for lengthy transport routes; or (ii) the rate mutually agreed to in interconnection negotiations.

Application of the default rate through a tariff would be the best approach. CMRS providers and ROR ILECs would still negotiate the many other terms and conditions of interconnection, which would be facilitated by the availability of a default target rate established by the Commission.

Establishing a reasonable default reciprocal compensation rates would also prevent the expansion of the difference between the rates paid by CMRS providers and IXCs. Allowing access rates to move toward reciprocal compensation rates would bring reciprocal compensation and access rates significantly closer and simplify later unification of those rates at an appropriate level.

Before the end of the transition period, the Commission should open an investigation to determine appropriate timelines and processes to unify all intercarrier compensation. Deferring portions of the process for ROR ILECs is supported by the difficulty of determining the level and effect of policy changes occurring more than three or more years in the future.

2. Compensation under the new intercarrier compensation restructuring mechanism should be based on all Commission required revenue reductions, less reasonable increases in local charges.

The new intercarrier compensation restructuring mechanism should provide compensation to ROR ILECs based on: (i) required reductions (measured from a base year) in interstate and intrastate access revenues, plus net reductions in intercarrier reciprocal compensation; less (ii) the amounts that can be recovered from reasonable additional local subscriber line charges ("SLCs"). The additional SLC should not exceed $1.50 per month in any year of the transition period and the cumulative additional SLCs plus the ROR ILEC's average mandatory local charges should not exceed the Statewide Residential Benchmarks (discussed below). For example, assume that the Statewide Residential Benchmark is $20.00 and the ROR ILEC's average mandatory local charges total $15.00. The maximum additional SLC would be $5.00 ($20.00 Statewide Residential Benchmark - $15.00 current charge). The maximum annual SLC increase would be $1.50 per line per month, so the $5.00 increase would occur over 4 years.

Further, if: (i) the ILEC incurred a total reduction of $6.00 per line per month from reductions in interstate and intrastate access revenues and net reductions in intercarrier reciprocal compensation (from the base year); and (ii) the reduction was phased in, in equal amounts, over a 3 year period, the ROR ILECs recovery from the intercarrier compensation restructuring mechanism would be as follows:

Yr	Reduction to Intercarrier compensation from base	:Less	Cumulative cap on SLC increases	:Equals	Intercarrier compensation restructuring mechanism recovery
1	$ 2.00		$ 1.50		$ 0.50
2	$ 4.00		$ 3.00		$ 1.00
3	$ 6.00		$ 4.50		$ 1.50
4	$ 6.00		$ 5.00*		$ 1.00

* Capped at specific ILEC increase required to equal the Statewide Residential Benchmark.

Eligibility for payments from the new mechanism should not require a showing that the ROR ILEC is unable to obtain replacement revenues from other sources.[51] Such a requirement would be impractical for the Commission to administer consistently and extremely costly (with over 1,000 differently situated ROR ILECs). State administration of processes requiring such a showing would suffer from even less consistency and no less cost. Further, ROR ILECs in many States operate under incentive and other alternative regulation (e.g. price cap) arrangement/plans that were premised on the basis that the ROR ILECs would be motivated to cut costs and thus avoid local rate increases in return for exemption from earnings regulation. Requiring such carriers to show inability to replace the revenues from other sources is just as inconsistent as requiring Price Cap ILECs to now justify their earnings. Such after-the-fact changes in the

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[51] *FNPRM* ¶ 109.

regulatory contract would be inappropriate and would impede the reform process with costly and time consuming legal contests.

3. Payments under the new intercarrier compensation restructuring mechanism should be made only to carriers that experience revenue reductions due to Commission required changes.

Payments under the new mechanism would for a specific purpose, the replacement of revenues reduced as a direct result of the Commission's decisions. Only carriers whose payments are reduced should be eligible to receive such payments, and those payments should not be portable to carriers that did not experience the reductions in their revenues.

Portability would add substantial costs by providing a revenue windfall for carriers that are not experiencing intercarrier compensation reductions. With the cost of the current USF already a significant issue, and the reduction of intercarrier compensation adding costs, funding from the new mechanism should be available only to carriers that actually experience a loss of revenues due to Commission required reductions in interstate and intrastate access revenues and reciprocal compensation.

Funding for the new intercarrier compensation restructuring mechanism should have a broad and stable base and should include the modifications to the current USF funding process discussed below in Section II.F.

4. The Commission should take additional reasonable steps to reduce other arbitrage opportunities and discrepancies.

The Commission should also take steps that limit other arbitrage opportunities and prevent the widening of other gaps in intercarrier compensation because ROR ILECS should continue to be paid for the use of the local network to originate and terminate traffic.

a. ROR ILECs should be compensated for terminating VoIP traffic on their networks.

VoIP traffic terminated to ROR ILEC networks, whether terminated directly or indirectly, should be subject to the same compensation requirements as other telecommunications traffic. If the traffic is identified as interexchange traffic, it should be subject to access charges, even if it is terminated through a local interconnection trunk or EAS arrangement. If the traffic is identified as local traffic, it should be subject to reciprocal compensation. If the VoIP provider delivers traffic without jurisdictional identification, such traffic should be subject, by default, to (interstate) access rates.

Some VoIP providers may also seek to evade all of the intercarrier compensation mechanisms by purchasing local retail access lines for the purpose of terminating traffic. By purchasing a local retail line, a VoIP carrier would be able to terminate all of its traffic as if it originated locally from a retail customer, escaping the payment of both access and reciprocal compensation. Such a practice would be particularly effective in an EAS situation, allowing the VoIP carrier to disguise its traffic as ILEC or CLEC traffic and thus terminate its traffic throughout the extended calling area without paying compensation. Such practices need to be strictly prohibited.[52]

Because the routing of VoIP traffic can be hidden by the telecommunications carrier providing the VoIP service, the Commission should take reasonable action to address and reduce

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[52] See, NARUC Plan, *FNPRM* Appendix B, page 5, ¶ II.C.

> C. No Covered Entity should be entitled to purchase a service or function at local rates as a substitute for paying intercarrier compensation.

the level of available arbitrage, and all VoIP traffic should provide at least some contribution toward the cost of maintaining the rural facilities needed to make the VoIP service viable.[53]

b. Dial-up ISP traffic[54] should not be subject to reciprocal compensation.

As previously discussed, requiring ROR ILECs to pay reciprocal compensation for termination of traffic to ISPs is likely to cause a severe increase in the costs of providing local service. These risks are exacerbated where there are expanded local calling services such as EAS. With only limited customer bases and already high network costs, ROR ILECs would be unable to absorb such cost increases. That combination of factors would virtually compel ROR ILECs to re-price EAS and other expanded local calling services that, in many cases, preceded local competition. The Commission should take the steps needed to avoid that result and exempt ROR ILECs from paying reciprocal compensation for ISP traffic, particularly traffic terminating in the local calling areas of other ILECs. Failure to do so is very likely to require repricing of expanded local calling arrangements, such as EAS, and would disrupt long- standing local service arrangements for many end users.[55]

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[53] Some plans, such as the ICF plan seek to solve the arbitrage problem by substituting a bill and keep approach. That approach is inappropriate for ROR ILECs and a far too radical solution to the problems posed by intercarrier compensation for ROR ILECs.

[54] The reference to ISP traffic is to traffic bound to an Internet service provider. An ISP is an entity that provides its customers the ability to obtain on-line information through the Internet. Declaratory Ruling in CC Docket No 96-98 and Notice of Proposed Rulemaking in CC Docket No. 99-68 at § 4.

[55] The ICF edge plan appears to require a change in existing compensation arrangements between ILECs in existing EAS areas, imposing transit service charges for use of EAS tandems. Such a change would be highly inappropriate and would require repricing of such plans and disruption of service to many local customers.

c. Virtual NXX traffic is not local traffic and should not be subject to reciprocal compensation.

Virtual NXX traffic is traffic that looks like local traffic to the calling customer because of the use of local numbers, but is actually interexchange traffic. Virtual NXX traffic provides no revenue to the ILEC in the exchange where the call originates, although it is interexchange traffic.

The Commission should not require the originating ILEC to pay reciprocal compensation on a call that would generate originating access revenues if it were carried by an IXC. If the Commission were to require reciprocal compensation for this traffic, it could have a huge financial impact on ROR ILECs and their customers.

One way to eliminate this form of arbitrage would be to subject Virtual NXX traffic to access charges. The calls originate and terminate in different exchanges and the carrier providing the Virtual NXX service acts as a toll carrier. In the MIC members' experience, almost all Virtual NXX is for dial-up ISP traffic. Use of Virtual NXXs provides significant economies to the ISP provider, which can centralize its operations into a single location. At a minimum, a carrier that avoids access charges (by offering Virtual NXX arrangement) should not be further rewarded by also receiving reciprocal compensation.[56]

[56] Further, if that carrier desires to purchase transport from the originating ROR ILEC for such traffic, the transport should be purchased off of the originating ILEC's access tariff (special access if a dedicated facility is used).

d. Revenue neutral capacity-based terminating access plans should be allowed.

The Commission invited comments regarding the replacement of per MOU access rates with capacity based rates.[57] Using capacity-based terminating access rates rather than minutes of use to recover the revenue requirement does not change the need to recover the same amount of revenue, but it may lead to improved efficiency, a goal recognized by the Commission,[58] and improved stability. ROR ILECs should be allowed to implement capacity-based terminating access plan that are designed to recover revenues comparable to per minute of use charges. Until there is experience demonstrating the successful application, either on an individual basis or through a NECA pooling process, such a plan should be voluntary, particularly during any intrastate access transition period for ROR ILECs.

D. <u>Both Annual Caps on Additional SLCs and Statewide Residential Benchmarks to Limit Cumulative SLC Increases Are Needed.</u>

The Commission noted that preservation of universal service objectives is central to the reformation of intercarrier compensation.[59] That approach is consistent with the fundamental policy established by Congress in 47 U.S.C. § 254(b)(3) that:

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[57] *FNPRM* ¶ 105. "We solicit comment on alternative approaches that would give LECs the opportunity to recover costs previously recovered from IXCs through interstate access charges. ... Parties that favor an approach based on flat-rated charges should be specific in identifying what costs should be recovered from IXCs, how these charges should be calculated, and the length of any transition period."

[58] *FNPRM* ¶ 31. "... Based on the record, we agree with commenters that any new approach should promote economic efficiency."

[59] *FNPRM* ¶ 32. "Preservation of universal service is another priority under the Act and we recognize that fulfillment of this mandate must be a consideration in the development of any intercarrier compensation regime. This Commission remains committed to universal service, and we are particularly sensitive to the interests of rural and high-cost communities. Given the relationship between intercarrier

> Consumers … in rural, insular, and high cost areas, should have access to telecommunications and information services, … at rates that are reasonably comparable to rates charged for similar services in urban areas.

To preserve this comparability, it is necessary to establish both annual caps on additional SLCs and cumulative limits on the total additional SLCs.

Annual caps are needed on additional SLCs because of the significant disparity that exists between local rates, which reflect a variety of factors, including very wide differences between the sizes of local calling areas. For example, in Minnesota local calling areas range in size from well under 1,000 access lines to over 2,000,000 access lines in the Minneapolis/St. Paul EAS area. The size of local calling area is often reflected in current rates and has a clear impact on affordability.[60] These local rate differences must be eliminated at a reasonable pace in order to prevent rate shock for local customers. The impact of annual caps on the new intercarrier compensation restructuring mechanism is not likely to be significant, because the number of customers at lower local rates is not substantial. In contrast, the impact on the individual customers of large local rate increases would be severe. These considerations should be resolved in favor of individual customers.

To control cumulative additional SLCs, the FCC should require each State Commission to establish a Statewide Residential Benchmark, which would be equal to the statewide weighted average RBOC Residential Rate as of January 1, 2005, including Federal and State Subscriber Line Charges, and mandatory local calling area charges. The Statewide Residential Benchmark

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compensation and universal service support, we recognize that reforms to the intercarrier compensation regime may warrant changes to universal service support mechanisms."

[60] *In the Matter of Federal-State Joint Board on Universal Service,* REPORT AND ORDER, 12 FCC Rcd. 8776, CC Docket 96-45, May 8, 1997, ¶¶ 112-113.

that would limit the amount a ROR ILEC could be required to pass on to their end users as a result of the Commission ordered changes to intercarrier compensation.

A Statewide Residential Benchmark is appropriate because rate levels vary between states, reflecting differences in calling areas, densities, line lengths and other state specific variables. A Statewide Residential Benchmark is also appropriate because it would preserve current state specific rate structures with which consumers are typically the most aware, thus providing greater consumer acceptance.

The Commission should adopt a uniform formula for the State Commissions to use in developing the Statewide Residential Benchmark to protect the new recovery mechanism from imposing a burden on the universal service fund from inconsistent methodologies between states. The formula should establish whether and how any adjustment to the Statewide Residential Benchmark should be made to reflect any Commission mandated changes to the January 1, 2005 RBOC rates. If each State Commission were to establish a benchmark absent well defined Commission guidelines, there would be significant differences state by state. Further, since the purpose of the Statewide Residential Benchmark is in large part to determine the amount of compensation that would be available from the new mechanism, the use of different methodologies could encourage the establishment of unreasonably low benchmark rates in order to receive additional compensation.

State Commissions should, however, oversee the calculation and certification of the Statewide Residential Benchmark. State Commissions would be in the best position to gather the necessary information and determine, test and certify the results to the Commission.

ROR ILECs should not be compelled to charge the additional SLCs which may not be sustainable due to the competitive situation in individual ROR ILECs particular markets, e.g., the existence of one or more traditional or broadband competitors, etc. Rather, an individual ROR ILEC should have the option of forgoing part or all of any additional SLC increase. Adverse impacts on the new mechanism would be prevented because a decision to forego some of all of an additional SLC would not increase the level of compensation available to the ROR ILEC from the new mechanism. Rather, the ROR ILEC's support from the new mechanism would be determined on the basis of the authorized additional SLC.

E. <u>ROR ILECs Should Not Be Required to Provide or Pay for Transport of Traffic Beyond Their Exchange Networks.</u>

ROR ILECs should not be required to interconnect with other telecommunications carriers outside of the ROR ILEC's end office local exchange network area. ROR ILECs and interconnecting carriers should be charged with the cost of providing and paying for facilities (subject to default or mutually agreed reciprocal compensation) on their respective sides of the interconnection point.

The requirements of Section 251(c)(2) of the Act set forth the ILEC's duty regarding interconnection. An ILEC has:

> The duty to provide … interconnection with the local exchange carrier's network—
> ***
> (B) at any technically feasible point within the carrier's network.

It may be technically feasible for an RBOC to provide a single point of interconnection for an entire LATA through an access tandem or its interconnected access tandems. With rare exceptions, ROR ILECs do not have such interconnected networks.

As a result, ROR ILECs should only be required to interconnect within their exchange networks.[61] The Commission should not take any steps that would require network or compensation changes to the current, common practice of interconnecting with ROR ILECs through third-party tandems and transport providers, including the operator of a centralized equal access tandem or transport provider.[62] Where there is sufficient traffic to justify a direct connection, the interconnection would be somewhere within the local exchange boundary of the

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[61] The intraMTA rule has fulfilled its purpose of assisting CMRS providers by relieving them from paying higher access rates. The intraMTA rule should be eliminated and should certainly not be applied to require ROR ILECs to deliver traffic beyond their local exchange areas or to pay reciprocal compensation to CMRS providers for traffic that is delivered by IXCs.

[62] The ICF edge plan establishes clear limitations on the interconnection and transport obligations of ROR ILECs that are Certified Rural Telecommunications Carriers (CRTCs). However, the ICF edge plan errs in that, when Centralized Equal Access (CEA) functionality is provided at a tandem, the tandem should not be treated differently than any other third-party tandem.

The ICF Plan makes one critical error when it assumes that the CRTC's network includes a CEA tandem. Like all other third-party tandems, the CEA tandem owner provides the facilities up to the ROR ILEC's network (generally the ROR ILEC's exchange boundary). The CEA tandem owner is independent from the ROR ILEC. It has separate ownership from the ROR ILEC, and charges its own CEA tandem and switching transport rates. There is no reason to single out CEA tandems for different treatment from other third-party tandems and to impose added costs on the ROR ILECs based on existing network arrangements.

Further, it appears based on the Edge Plan details, that a carrier with any significant volume of traffic, that has interconnection with a CRTC, could escape paying the CRTC default transport charge and possibly force the CRTC into a position of not only having to forgo this charge but in fact having to pay the interconnecting carrier the default amount. This would result in a situation worse than bill and keep for the CRTC since they would not only have no transport revenues but could be forced to pay the Interconnecting Carrier for transport. Because of the possibly significant and currently unknown impacts for individual ROR ILECs, a comprehensive examination of the Edge Plan would be needed. The complexity of the Edge Plan dictates that this would best be accomplished outside a normal comment process such as through a less-traditional approach.

ROR ILEC. Where the ROR ILEC operates a tandem, it would be at an ROR ILEC tandem, allowing access to all end offices subtending that tandem.

These results are required by the Act, and are reasonable and practical results. ROR LECs should not be required to either provide or pay for transport to each interconnecting telecommunications carrier's preferred location. LATAs can cover hundreds of miles, and there can be dozens of potential interconnecting carriers (CMRS, Virtual NXX, CLEC, VoIP, all claiming to need to exchange local traffic). The cost and burden of allowing each such carrier to establish its desired point of presence ("POP") and requiring every ROR ILEC in the state to deliver traffic to that POP would be incredibly costly, unnecessary and burdensome. There is already an existing and economical network available for seeking such indirect interconnection. These interconnecting carriers should make arrangements with and pay third party transport and tandem switching providers for such service for their originating and terminating traffic. If the CMRS, Virtual NXX, CLEC, or VoIP provider determines that it wants to provide local service in, or exchange traffic with an ROR ILEC's service area, the cost of establishing a local interconnection for that traffic should be borne by that carrier, not the ROR ILEC.

In addition, if the ROR ILEC's network were determined to extend to the CEA tandem (as the ICF Plan suggests), this would create a possible single point of interconnection for an entire state and put the full cost of transport to the location on the ROR ILEC. Similarly, the ROR ILECs network should not be determined to include any third-party transport provider's facilities. Including such third-party networks would be unreasonable interpretations of the ROR ILEC network, and depending on whether ROR ILECs would be allowed to charge for the cost of transport to and from the CEA or transport facilities, would have unreasonable cost consequences. The existing interconnection responsibilities related to CEA tandems and using third-party transport facilities should not change as a result of this docket.

F. Universal Service Reform Should Be Part of Intercarrier Compensation Reform.

ROR ILECs have three sources of revenue: (i) local rates; (ii) intercarrier compensation; and (iii) support mechanisms. These comments have suggested changes to both intercarrier compensation and local rates and proposed the establishment of a new intercarrier compensation restructuring mechanism to address revenue shortfalls that result from the limits to SLC increases. In addition, in order to achieve universal service objectives, the existing Universal Service Fund ("USF") should be strengthened. More specifically, the Commission should: (a) eliminate the existing USF cap; (b) broaden and stabilize the base for contributions to the existing USF rules on the same basis as the new intercarrier compensation restructuring mechanism (e.g., numbers or connections used, etc.); and (c) institute a proceeding to ensure appropriate support for broadband in rural areas.

Currently contributions to the USF are based on interstate revenues only. Using revenues as the basis for determining support levels is unsustainable because interstate revenues are declining and the jurisdictional identification of revenues is too easy to manipulate and too difficult to enforce, creating unequal burdens between carriers. Therefore, a broader, more uniform basis for determining support obligation is needed.

III. CONCLUSION

The Commission should take a pragmatic approach and focus on practical and timely steps that provide material progress toward the unification of intercarrier compensation rates. The Commission must also assume responsibility that corresponds to the scope of the changes that it initiates. If the Commission requires reform of intrastate access rates and other intercarrier compensation (as it should), it is essential for the Commission to also provide mechanisms allowing replacement of the resulting reductions in revenue.

The Commission should adopt separate approaches and separate transitions for Price Cap ILECs and ROR ILECs because their financial characteristics, and the resulting financial impacts of reform, vary so widely. Because of these financial characteristics and impacts, bill and keep should not be adopted for ROR ILECs. If the Commission's decisions do not recognize and accommodate these differences, significant delays or harm to customers in rural areas will occur.

ROR ILECs do not typically own the interexchange network facilities and are often far removed from tandems and other facilities of other indirectly interconnected carriers. The cost of providing transport beyond their local exchange networks would add substantially to their already much higher network costs. As a result, ROR ILECs should not be required to provide or pay for transport of traffic beyond their local exchange networks.

Respectfully submitted,

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